# FISCAL NOTE

# SB 1504 - HB 1399

February 19, 2007

**SUMMARY OF BILL:**     Enacts the "Health Care Assistance Act of 2007," effective July 1, 2007.  Increases the excise tax on cigarettes from 20 cents to 60 cents per pack.  Increases the excise tax on cigarettes by 1 cent per pack in each fiscal year ending in an even number, beginning with FY07-08 and continuing until FY17-18.  Creates a "Health Care Assistance Account (HCAA)" within the state treasury.  Requires all funds generated from such tax increase be deposited into the HCAA and used to assist families with extraordinary health expenses.

## ESTIMATED FISCAL IMPACT:

**Increase State Revenues:**
        $223,632,000 / Health Care Assistance Account
         $3,242,000 / General Fund
         $7,272,000 / Education Fund
           $41,000 / Department of Revenue
          $103,000 / Sinking Fund
         $234,290,000 – Total Revenue Increase

**Increase State Expenditures - $220,000 Recurring**
                        **$200,000 One-Time**

**Increase Local Govt. Revenues - $4,104,000**

   Cigarette Tax Assumptions:

- According to the DOR, excise tax collections on cigarettes in FY05-06 were approximately $115,462,000.
- Current excise tax rate on cigarettes is $0.20 per pack.
- Estimated number of packs sold in FY05-06 was 577,310,000 ($115,462,000 ÷ $0.20 = 577,310,000 packs).
- Cigarette elasticity is estimated from a variable elasticity schedule depending upon the extent of any excise tax increase.
- Cigarette elasticity rate for proposed increase is estimated to be -0.288.
- Current state sales tax rate on cigarettes is 7.00%.

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- Local option sales tax rate on cigarettes is estimated to average 2.25%.
- Current consumer price per pack is estimated to be $3.19 per pack (excluding sales tax); $3.49 per pack (including sales tax).
- Increasing the excise tax on cigarettes by $0.41 per pack ($0.40 one-time + $0.01 annual = $0.41 increase in FY07-08) would also generate an additional $0.04 per pack in state and local option sales tax revenue ($0.41 X 9.25% = $0.038).
- The total price increase to the consumer is estimated to be $0.45 per pack ($0.41 excise tax increase + $0.04 incremental sales tax = $0.45).
- Consumer price per pack after the proposed excise tax increase is estimated to be $3.60 per pack (excluding sales tax); $3.94 per pack (including sales tax).
- Increasing the excise tax on cigarettes would increase the price per pack to the consumer by an estimated 12.89% ($0.45 ÷ $3.49 = 12.89%).
- Quantity demanded would decrease by an estimated 3.71% (12.89% price increase X -0.288 elasticity rate = -3.71%).
- Quantity demanded in FY07-08 is estimated to be 555,891,800 packs (577,310,000 X {100.00% - 3.71%} = 555,891,799).
- Total excise tax collections are estimated to be $339,094,000 (555,891,800 packs X $0.61 excise tax = $339,093,998) in FY07-08.
- Incremental excise tax collections are estimated to be $223,632,000 ($339,094,000 - $115,462,000 = $223,632,000) per year.
- 100% of the estimated $223,632,000 in incremental excise tax collections would be apportioned exclusively to the HCAA.
- Excise tax collections would grow in subsequent fiscal years due to the additional excise tax rate increases proposed in this legislation.
- Sales tax collections will increase because sales tax is computed on the final retail sale (which includes any current and increased excise tax).
- Retail sales before the proposed excise tax increase are estimated to be $1,841,619,000 (577,310,000 packs X $3.19 old price (excluding sales tax) = $1,841,618,900).
- Retail sales after the proposed excise tax increase are estimated to be $2,001,210,000 (555,891,800 packs X $3.60 new price (excluding sales tax) = $2,001,210,480).
- Incremental retail sales are estimated to be $159,591,000 ($2,001,210,000 - $1,841,619,000 = $159,591,000).
- Incremental state sales tax revenue is estimated to be $11,171,000 ($159,591,000 X 7.00% state rate = $11,171,370) per year.
- The $11,171,000 in incremental state sales tax revenue would be apportioned as follows: $3,242,000 to the General Fund, $7,272,000 to education, $513,000 to local governments, $41,000 to the DOR, and $103,000 to the Sinking Fund.
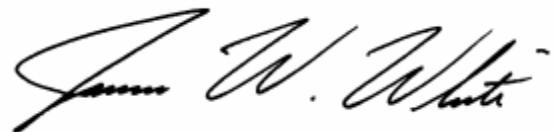
- The net recurring increase to state revenues resulting from incremental state sales tax collections is estimated to be $10,658,000 ($11,171,000 - $513,000 local share = $10,658,000) per year.
- Additional sales tax revenue will result (for both state and local governments) in subsequent fiscal years due to the additional excise tax rate increases proposed in this legislation.
- The total net recurring increase to state revenues resulting from the increased excise tax is estimated to be $234,290,000 ($223,632,000 from additional excise tax + $10,658,000 from additional sales tax = $234,290,000) per year.
- Incremental local option sales tax revenue is estimated to be $3,591,000 ($159,591,000 X 2.25% local option rate = $3,590,798).
- The total net recurring increase to local government revenues resulting from the increased excise tax is estimated to be $4,104,000 ($3,591,000 in local option tax revenue + $513,000 in state-shared sales tax revenue = $4,104,000).

Other Assumptions

- Three additional Regulatory Officers in the DOR will be required to combat the illegal importation of cigarettes into Tennessee.
- Security upgrades will be required for cigarette tax stamps to combat illegal/counterfeit tax stamps.
- The recurring increase to state expenditures for the new positions and tax stamp enhancements is estimated to be $220,000 per year.
- The one-time increase to state expenditures for computer and software enhancements and for costs associated with hiring the three Regulatory Officers is estimated to be $200,000.
- It is the legislative intent that the fiscal impact of this bill be as revenue-neutral as practicable in the immediate and long-term. However, this legislation as proposed includes no language that reduces tax elsewhere to achieve the revenue-neutral intent.

## CERTIFICATION:

This is to duly certify that the information contained herein is true and correct to the best of my knowledge.

*James W. White*

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James W. White, Executive Director

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